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Nos. 86-1598 & 86-1615

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

KAISER ENGINEERS, DIVISION OF HENRY J. KAISER COMPANY, and AZL ENGINEERING, INC. (formerly SERGENT HAUSKINS & BECKWITH),
Petitioners,

v.

ALLENDALE MUTUAL INSURANCE COMPANY,
Respondent.

On Petitions for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

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RESPONDENT'S BRIEF IN OPPOSITION

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QUESTION PRESENTED

Where an insurer has been adjudged liable to its insured, has appealed the judgment, and is in imminent danger of losing its subrogation rights through the running of a statute of limitations, does a dispute between the insurer and tortfeasors potentially liable to the insurer by way of subrogation constitute an "actual controversy" of sufficient immediacy and reality to support jurisdiction under the Declaratory Judgment Act and Article III, Section 2, of the Constitution?

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RESPONDENT'S BRIEF IN OPPOSITION

The respondent, Allendale Mutual Insurance Company,[1] respectfully submits this brief in opposition to the peti-

[1] In compliance with Sup. Ct. R. 28.1, Allendale states that it has no parent companies and that all subsidiaries of Allendale are wholly-owned, except for the following affiliates: FM Insurance Company Limited, Factory Mutual Engineering Corporation, and Factory Mutual Service Corporation. Allendale is a partner in the Factory Mutual Engineering Association and the Factory Mutual Service Bureau.

tions for a writ of certiorari to the United States Court of Appeals for the Tenth Circuit filed by Kaiser Engineers, Division of Henry J. Kaiser Company, and AZL Engineering, Inc. (formerly Sergent Hauskins & Beckwith). The decision of the Court of Appeals entered on November 6, 1986, is reported at 804 F.2d 592 (10th Cir. 1986), and is reprinted in Appendix A to each of the petitions.[2]

STATEMENT OF THE CASE

The losses from which this jurisdictional dispute arises occurred at a uranium mill owned and operated by Allendale's insured, United Nuclear Corporation ("UNC"). In July 1979, a uranium wastewater retention dam at UNC's mill collapsed, releasing large quantities of hazardous waste and interrupting UNC's milling operations. The retention dam had been designed and built by petitioners Kaiser Engineers and AZL Engineering ("Kaiser/AZL"). To recover its losses, UNC sued Allendale in a New Mexico state court, alleging it was entitled to reimbursement under a policy of business interruption and property damage insurance. The trial court resolved the coverage dispute in UNC's favor and awarded UNC $24,670,724 in compensatory damages and $25,000,000 in punitive damages. Judgment for these amounts was entered against Allendale on May 27, 1983, and Allendale appealed to the Supreme Court of New Mexico.[3]

In New Mexico property damage claims are subject to a four-year statute of limitations. N.M. Stat. Ann. § 37-1-4 (1978). Fearing that this statute might run and bar

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[2] In this brief, appendix citations will be to pages in the appendices to the AZL Engineering, Inc. petition and will be in this form: "AZL Pet. App. ——."

[3] On October 15, 1985, the New Mexico Supreme Court affirmed the award of compensatory damages and reversed the award of punitive damages. *United Nuclear Corp. v. Allendale Mut. Ins. Co.*, 103 N.M. 480, 709 P.2d 649 (1985).

assertion of subrogation claims against Kaiser/AZL in the event UNC's judgment were upheld on appeal, Allendale filed the present declaratory judgment action on July 15, 1983, in the United States District Court for the District of New Mexico. Allendale sought a declaration that UNC's losses were caused by Kaiser/AZL's negligence and that it was entitled to recover from them all sums which it might be required to pay UNC under the contract of insurance.

The District Court dismissed Allendale's complaint on the ground that, because Allendale had not yet paid the UNC judgment, it was not subrogated to UNC's right of action against Kaiser/AZL. The District Court concluded that an "actual controversy" did not exist under 28 U.S.C. § 2201, and that it lacked subject matter jurisdiction to entertain the action. AZL Pet. App. 8.

Allendale appealed from the dismissal of its complaint, and on November 6, 1986, the United States Court of Appeals for the Tenth Circuit reversed. The Court held that an "actual controversy" did exist between Allendale and Kaiser/AZL and remanded the case for further proceedings. AZL Pet. App. 1. Kaiser/AZL's petitions for rehearing were denied January 2, 1987. AZL Pet. App. 11.

The dispute in the District Court over the extent of Allendale's subrogation rights is now moot because the New Mexico Supreme Court affirmed UNC's judgment for compensatory damages and in December 1985 Allendale paid that judgment. Thus, Allendale is now fully subrogated to UNC's right of action against Kaizer/AZL. After remand to the District Court, Allendale amended its complaint asserting that it had paid the UNC judgment and seeking damages against Kaizer/AZL by way of subrogation. The present dispute over the District Court's jurisdiction at the time Allendale originally filed its declaratory judgment action would also be moot but for the possibility that the New Mexico statute of limitations

might bar Allendale from now filing a new action against petitioners.

REASONS WHY THE PETITIONS SHOULD BE DENIED

I. The Court of Appeals Correctly Applied *Maryland Casualty* to the Facts of This Case, and the Decision Below Does Not Pose a Federal Question of Substantial Importance.

The Court of Appeals applied this Court's holding in *Maryland Casualty Co. v. Pacific Coal & Oil Co.*, 312 U.S. 270 (1941), to the facts of this case and correctly concluded that there was an actual controversy of sufficient immediacy and reality to support the District Court's jurisdiction under the Federal Declaratory Judgment Act.

In *Maryland Casualty*, this Court held that under the Declaratory Judgment Act, 28 U.S.C. § 2201 (Supp. III 1985), an "actual controversy" can exist between an insurer and a third party even though any obligation of the insurer to the third party is contingent upon the outcome of litigation pending in another court. The insurer in *Maryland Casualty* sought a declaration that it was not liable to a third party who had been involved in an automobile accident with its insured. The third party argued that an "actual controversy" did not exist because any liability of the insurer to the third party was contingent upon the outcome of pending litigation in a state court between the third party and the insured.

In rejecting this argument, this Court set forth the following test for determining whether an "actual controversy" exists:

> The difference between an abstract question and a "controversy" contemplated by the Declaratory Judgment Act is necessarily one of degree, and it would be difficult, if it would be possible, to fashion a precise test for determining in every case whether there

> is such a controversy. Basically, the question in each case is whether the facts alleged, under all the circumstances, show that there is a substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality to warrant the issuance of a declaratory judgment.

312 U.S. at 273.

The situation here is similar to that in *Maryland Casualty*. Here the insurer, Allendale, sought a declaration that third parties, Kaiser/AZL, would be liable to Allendale contingent upon the outcome of pending state-court litigation. Kaiser/AZL argue that an actual controversy did not exist at the time this action was filed because Allendale's right to recover from Kaiser/AZL was contingent upon affirmance of the state-court judgment. The only significant distinction between this case and *Maryland Casualty* is that *Maryland Casualty* involved an insurer's contingent *liability* to a third party, depending upon the outcome of other litigation, while this case involves an insurer's contingent *claim* against a third party, depending upon the outcome of other litigation. Declaratory relief is no less appropriate in asserting a contingent claim than in resisting a contingent liability.

Kaiser/AZL take the position that declaratory relief is inappropriate when future events, like reversal of the state-court judgment in this case, may extinguish a contingent claim for money damages. Petitioners plainly confuse the ultimate right of recovery, in this case money damages, with the right to obtain a declaration of the rights of the parties. Petitioners ignore the express language of 28 U.S.C. § 2201(a) that declaratory relief may be obtained "whether or not further relief is or could be sought."

Petitioners, particularly Kaiser Engineers, argue that, by permitting a declaration of Allendale's rights, the Tenth Circuit has created an entirely new type of action, which if allowed to stand will engulf the federal

courts in unnecessary litigation. On the contrary, the decision below establishes no new legal principles and gives rise to no new causes of action. Instead, the Tenth Circuit has carefully applied to the circumstances of this case the doctrine established over fifty years ago in *Maryland Casualty*. Petitioners ignore this Court's recognition in that case that a need for declaratory relief may exist even in the absence of a present right to recover damages.

Federal Courts have long exercised jurisdiction over contingent rights of recovery. For example, Fed. R. Civ. P. 14(a) provides that a defendant may implead a person "who is or may be liable to him for all or part of the plaintiff's claim against him." In particular, an insurer is entitled to implead a third-party tortfeasor who the insurer alleges will be liable to it for any sum the insurer is required to pay to its insured, even though the insurer's subrogation rights have not yet been perfected by payment to the insured. *Glens Falls Indem. Co. v. Atlantic Bldg. Corp.*, 199 F.2d 60, 63 (4th Cir. 1952). In light of this long-standing recognition of the authority of federal courts, petitioners cannot argue now that exercising jurisdiction over such contingent rights of recovery violates the "case or controversy" requirement of Article III of the Constitution.[4]

In determining whether an "actual controversy" exists under the Declaratory Judgment Act, a plaintiff's need for a declaration of his rights is of decisive importance. *Eccles v. Peoples Bank of Lakewood Village, Cal.*, 333 U.S. 426, 431 (1948). In *Maryland Casualty* the Court was concerned with the insurer's need to avoid possible conflicting interpretations of its insurance policy. In this

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[4] The "actual controversy" language in the Declaratory Judgment Act requires that a "case or controversy" exist under Article III of the Constitution. *Aetna Life Ins. Co. v. Haworth*, 300 U.S. 227, 239-40 (1937). AZL Engineering concedes this. AZL Pet. 7. Therefore, if an "actual controversy" exists as defined by this Court in *Maryland Casualty*, then a "case or controversy" also is present under Article III.

case the insurer's need is of even greater immediacy and reality. If Allendale were denied declaratory relief, its subrogation claims might be barred by New Mexico's four-year statute of limitations. Concern for the running of a statute of limitations has been held to be "the kind of interest that the Declaratory Judgment Act was intended to protect." *Fidelity & Deposit Co. of Maryland v. City of Sheboygan Falls*, 713 F.2d 1261, 1265 (7th Cir. 1983). Moreover, the state-court judgment against Allendale was not remote, hypothetical or abstract; in order to stay it pending appeal Allendale had to post a supersedeas bond guaranteeing payment if the judgment were upheld. At the time this action was filed Allendale was thus faced with a trial-court judgment of nearly $25 million in compensatory damages and with the imminent running of the statute of limitations. Allendale's need for a determination of its rights was both immediate and real.

Maryland Casualty declares that the parties to a declaratory judgment action should have "adverse legal interests." 312 U.S. at 273. As soon as the state trial court entered judgment against Allendale, Allendale acquired a direct subrogation interest in its insured's right of action against Kaiser/AZL. *Meredith v. The Ionian Trader*, 279 F.2d 471, 474 (2d Cir. 1960): "To obtain the benefits of the doctrine of subrogation one of the conditions which the insurer must fulfill is payment, or *sufferance of a judgment requiring payment*, of the obligation owed the insured." (emphasis added)

Kaiser erroneously argues that New Mexico law confers a subrogation interest only when an insurer makes payment to its insured. Kaiser Pet. 10. On the contrary, a contingent subrogation right arises in favor of an insurer once a loss occurs, even though payment has not been made. *March v. Mountain States Mut. Cas. Co.*, 101 N.M. 689, 691-92, 687 P.2d 1040, 1042-43 (1984): "Although the subrogation right is not fixed until a loss payment is made, a contingent subrogation right in favor of the insurer arises when the loss occurs." Petitioners

once again confuse the interest necessary to recover damages with the interest necessary to obtain a judgment declaring the rights of the parties. A suit for declaratory relief to determine the extent and consequences of Allendale's contingent subrogation right is entirely consistent with New Mexico law.

II. No Conflict Exists Among the Circuit Courts of Appeals.

In 1948 this Court issued a writ of certiorari in *Maryland Casualty* to resolve a conflict then existing among the circuits respecting whether a dispute between an insurer and a third party constituted an "actual controversy" under the Declaratory Judgment Act. This Court resolved that conflict by fashioning a test which the Tenth Circuit routinely applied to the facts of this case. Today, there is no conflict among the circuits on this issue, and petitioners cite no cases establishing one.

Maryland Casualty has been consistently cited and repeatedly followed by federal courts in upholding declaratory judgment jurisdiction in cases involving contingent rights and liabilities. *E.g., American Machine & Metals v. De Bothezat Impeller Co.*, 166 F.2d 535, 536 (2d Cir. 1948) (action to determine legal consequences if party should exercise right to terminate written agreement); *Franklin Life Ins. Co. v. Johnson*, 157 F.2d 653, 658 (10th Cir. 1946) (dispute between insurer and contingent third-party beneficiary under life insurance policy)[5]; *Spivey v. Travelers Ins. Co.*, 407 F. Supp. 916, 917

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[5] AZL Engineering attempts to portray a conflict *within* the Tenth Circuit. AZL Pet. 23-24. To the contrary, in *Franklin Life* the Tenth Circuit cited *Maryland Casualty* and held:

> To hold a person whose interest is contingent may not be compelled to defend an action for a declaratory judgment would greatly diminish the field and lessen the utility of declaratory judgment actions.

157 F.2d at 658. The decision below does not conflict with any other Tenth Circuit decision except perhaps *National Valve & Manufacturing Co. v. Grimshaw*, 181 F.2d 687 (10th Cir. 1950), which, to the extent of any conflict, was expressly disapproved. AZL Pet. App. 7.

(E.D.Pa. 1976) (declaratory relief allowed even though underlying judgment appealed and not yet affirmed); *Lumbermens Mut. Cas. Co. v. Borden Co.*, 241 F. Supp. 683, 701 (S.D.N.Y. 1965) (subrogation rights contingent upon future finding that certain releases were invalid).

Though not citing *Maryland Casualty*, other federal courts also have held that an actual controversy may exist so as to justify declaratory relief even when the actual right of recovery is contingent upon future events. *E.g., Seguros Tepeyac, S.A. Compania Mexicana v. Jernigan*, 410 F.2d 718, 728-29 (5th Cir.), *cert. denied*, 396 U.S. 905 (1969) (dispute over insurer's duty to reimburse insured for future payments insured might be required to make to judgment creditor); *West American Ins. Co. v. Allstate Ins. Co.*, 295 F.2d 513, 516 (10th Cir. 1961) (dispute between two insurance companies over primary liability for future damages insured might be required to pay); *Pennsylvania Cas. Co. v. Upchurch*, 139 F.2d 892, 893-94 (5th Cir. 1943) (dispute between insurer and third-party claimant against insured when liability of insured not yet established).

The authors of the major treatises on federal civil procedure also have interpreted this Court's decision in *Maryland Casualty* to recognize an insurer's need to determine liability even though future contingencies may extinguish the actual right of recovery. *See* 10A C. Wright, A. Miller & M. Kane, *Federal Practice & Procedure* § 2757 at 586 (2d ed. 1983) ("It is clear that in some instances a declaratory judgment is proper even though there are future contingencies that will determine whether a controversy ever actually becomes real."); 6A J. Moore, J. Lucas & G. Grotheer, *Moore's Federal Practice* ¶ 57.19 at 57-203 (2d ed. 1986).

Kaiser Engineers incorrectly argues that the decision of the Seventh Circuit in *Fidelity & Deposit Co. of Maryland v. City of Sheboygan Falls*, 713 F.2d 1261 (7th Cir. 1983), conflicts with the decision below. Kaiser Pet. 6-9.

In fact, however, that decision *supports* the result reached by the Tenth Circuit. In *Fidelity* the Seventh Circuit granted declaratory relief to an insurer to determine its liability under a surety bond and its contingent claims against certain contractors whose work was insured by the bond. The Seventh Circuit *approved* the need for declaratory relief, noting that the passage of time might otherwise bar the insurer's claims. 713 F.2d at 1265.

The cases cited by Kaiser/AZL establish only that a controversy may be so remote that the issuance of declaratory relief is not warranted. Allendale does not dispute this obvious proposition. Under *Maryland Casualty*, whether an "actual controversy" exists requires a determination whether the facts alleged, under all the circumstances, establish a dispute of sufficient immediacy and reality to warrant declaratory relief. 312 U.S. at 273. Thus decisions in the circuit courts of appeals must be reviewed in light of the facts of each case. Petitioners cite no case, and Allendale is aware of none, in which a judgment has been entered against an insurer and the insurer has then been barred from seeking declaratory relief against one claimed to be liable to it merely because the outcome of an appeal from the judgment is still in doubt. Such a result would be in clear conflict with the principles articulated by this Court in *Maryland Casualty*.

III. The Decision Below Does Not Interfere with State Court Proceedings.

The petition filed by Kaiser Engineers maintains that the decision of the Court of Appeals constitutes an unwarranted intrusion into the affairs of the New Mexico court system and "overrides New Mexico state subrogation law. . . ." Kaiser Pet. 10. Kaiser relies upon *Colorado River Water Conservation Dist. v. United States*, 424 U.S. 800 (1976), and *Brillhart v. Excess Ins. Co. of America*, 316 U.S. 491 (1942), where this Court held that maintaining a federal suit may be inappropriate when a pending state-court action presents the same issues.

The decision below does not present this Court with any such situation. The state-court litigation between Allendale and UNC concerned the existence of insurance coverage under a policy issued to UNC. The federal action for declaratory relief between Allendale and Kaiser/AZL concerns the negligence of Kaiser/AZL in designing and constructing the uranium wastewater retention dam. These issues are separate and unrelated.

Kaiser argues that Allendale should have litigated both issues in one state-court action.[6] Kaiser Pet. 8. Allendale does not deny that under N.M. R. Civ. P. 14 it could have impleaded Kaiser/AZL into the state-court dispute over insurance coverage, but that rule, like the analogous federal rule, provides that a defendant "may" implead a party who may be liable to him. As the decision below held, impleading third parties is not mandatory. AZL Pet. App. 7 n.2. *See Salazar v. Murphy*, 66 N.M. 25, 31, 340 P.2d 1075, 1079 (1959). *Cf.* 3 J. Moore, *Moore's Federal Practice* ¶ 14.06 at 14-38 (2d ed. 1985) ("Impleader is permissive and not compulsory."); 6 C. Wright & A. Miller, *Federal Practice & Procedure* § 1446 at 245 (1971) (Rule 14 "does not compel defendant to bring third parties into the litigation . . . ."). Because the issues involved in the state and federal actions were unrelated, and because of the size and complexity of the litigation, Allendale elected to file a separate action in federal court. No state-court claim concerning Kaiser/AZL's liability or responsibility for the loss was pending. Therefore, Allendale's choice of a federal forum does not conflict with this Court's holdings in *Brillhart* or *Colorado River Water Conservation District.*

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[6] This argument, of course, is inconsistent with Kaiser's principal contention in its petition—that there was no case or controversy to litigate. It is precisely *because* Allendale had a cause of action for contingent relief against Kaiser/AZL—because such a justiciable controversy existed—that Allendale was entitled to sue them in *either* federal court (assuming diversity) or state court. *See also* p. 6, *supra.*

The right to a federal forum for Allendale's claims against Kaiser/AZL is provided by 28 U.S.C. § 1332 (1982). *Meredith v. City of Winter Haven*, 320 U.S. 228, 234 (1943): "The diversity jurisdiction was not conferred for the benefit of the federal courts or to serve their convenience. Its purpose was generally to afford to suitors an opportunity in such cases, at their option, to assert their rights in the federal rather than in the state courts." One of the prime purposes of the Declaratory Judgment Act was to permit an insurer to establish liability. *Western Cas. & Sur. Co. v. Teel*, 391 F.2d 764, 766 (10th Cir. 1968). Federal jurisdiction may not be refused merely because a state remedy is available or because another suit, involving other issues, is pending in a state court. *Id.*

CONCLUSION

The Court of Appeals correctly concluded that, when a judgment has been entered against an insurer who is awaiting the outcome of an appeal from that judgment, and when in that process the insurer is confronted with the running of a statute of limitations and loss of its subrogation rights against a potentially liable third party, an actual controversy of sufficient immediacy and reality exists to support an action by the insurer for declaratory relief. For the foregoing reasons, Allendale respectfully requests that the petitions for a writ of certiorari be denied.

Respectfully submitted,

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